even below the market rate, during periods of crisis and depression. Let the brakes of high rediscount rates be set early, long before the bottom of the hill is reached; and let the accelerating force of low rates be applied with similar promptness and decision. If the market rate is kept in harmony with the natural rate, violent changes in the general price level can scarcely occur.

# Agricultural and Commercial Loans

## A Comparison of Loans Made in a Great Agricultural State with Loans to the Largest Bank and to Member Banks in the Largest City in the Seventh Federal Reserve District

By J. B. McDOUGAL
Governor, Federal Reserve Bank of Chicago

IT would be too much to expect the general public to have more than a casual comprehension of banking or of the relations of the Federal Reserve Banks to other banks or to business. It is not expected that the public will understand the operations of a factory which makes electrical machinery or of the electrical machines that are made. Still any well informed man may know in a general way what a dynamo is and have a grasp of what is meant by horse power. So might he know that a bank in a great central city probably generates a large horse power in credit and that comparison of the operations of such a bank with those of any smaller bank can be valuable or informative only if relative size is considered.

In this country there are banks of all kinds and sizes. The customary method of grading banks is by "capital. and surplus," and "deposits." It takes 40 banks with $25,000 capital each to measure up in capitalization to one with $1,000,000. It takes 400 such banks to equal a $10,000,000 institution. If the comparative figures are carried far enough, and total resources are used as the basis, it will be found that there are single banks in New York and Chicago with resources larger than the combined resources of all member banks in certain individual states or perhaps in several states.

These large banks have as customers many small banks, as well as individuals and corporations. When borrowing from the Federal Reserve Banks, their transactions are usually in large amounts. It is natural that what is considered moderate borrowing for a large bank should appear extravagant when compared with the amount borrowed by a small bank. A loan of fifty million dollars appears very large when compared with one of fifty thousand. Relatively, however, fifty millions may be much more moderate than fifty thousand, if due consideration is given the respective reserve balances maintained with the Federal Reserve Bank by the institutions involved.

For instance, an officer of a country bank called at the Reserve Bank one day and asked for an additional loan. At the time his bank had become so extended that its excessive borrowings had been the subject of considerable correspondence. He was told that a definite limit must be placed on his borrowings at a point not far from the amount already borrowed. The country banker was piqued. He called at-

tention to the many millions loaned to some of the Chicago banks. The country bank's debt was less than two hundred thousand. A comparison was made at once. It was found that on the basis of reserve deposits the big banks might have owed the Federal Reserve Bank nearly three times as many millions if they had borrowed in the same proportion as the small bank.

A part, at least, of the criticism of the operations of the Reserve Banks during the recent trying times seems to be based on instances of similar misconception of facts and figures. A moderate borrowing by a large bank may appear out of proportion when compared to an actually excessive borrowing by a small bank, if only absolute figures are used.

In connection with the work of the Joint Committee on Agricultural Inquiry, which was instructed to "investigate . . . the banking and financial resources and credits of the country, especially as affecting agricultural credits," the Federal Reserve Bank of Chicago made a careful study of its loans to member banks. The purpose was to ascertain if there had been any discrimination, real or apparent, against banks serving agricultural communities.

Section 4 of the Federal Reserve Act was kept in mind. This section, in outlining the duties of directors of Federal Reserve Banks, provides as follows:

> Said board shall administer the affairs of said bank fairly and impartially and without discrimination in favor of or against any member bank or banks and shall, subject to the provisions of law and the orders of the Federal Reserve Board, extend to each member bank such discounts, advancements and accommodations as may be safely and reasonably made with due regard for the claims and demands of other member banks.

The study developed some interesting facts that are pertinent to this discussion. The loan records of commercial banks are not kept in such form that borrowers can be classified by occupations in any comprehensive way. It is true that for some time past Federal Reserve Banks have required member banks in their applications for rediscount to specify the business of customers whose notes are offered. But this information provides no adequate measure of the extent of the service rendered to agriculture. It is well known that many country banks make a practice of using their farmers' paper for rediscount only after exhausting their supply of other eligible paper which is presumably better known at the Federal Reserve Bank, such as, "commercial paper" and notes secured by United States government obligations.

No statistics are available to show the absolute amounts loaned to various industries, but the Federal Reserve Bank of Chicago was able, by a comparison of its loans to member banks, to obtain conclusive evidence that it had not discriminated against agriculture. Loans to and reserve deposits of member banks in a preëminently agricultural state were compared with similar figures for member banks in the other states as well as the largest cities in the district.

One of the tabulations made is printed in full on page 201 and presents an interesting comparison of the relative borrowings by all member banks in the preëminently agricultural state with all member banks in the city of Chicago and with the individual bank whose borrowings exceeded those of any other bank in the Federal Reserve District.

The table on page 201 includes percentages, showing the ratio of amounts borrowed to reserve deposits kept in the Federal Reserve Bank, a method

LOANS TO ALL MEMBER BANKS IN A GREAT AGRICULTURAL STATE COMPARED WITH LOANS TO THE LARGEST BORROWING BANK IN THE SEVENTH FEDERAL RESERVE DISTRICT AND LOANS TO ALL MEMBER BANKS IN THE CITY OF CHICAGO; ALSO, COMPARATIVE RESERVE DEPOSIT FIGURES.

(In thousands of dollars)

| | | All member banks in Agricultural State | Largest borrowing bank in the District | All member banks in Chicago |
|---|---|---|---|---|
| July 2, 1920 .... | *Reserve Deposit | 21,000. | 32,000. | 135,000. |
| | Loans | 63,000. | 80,000. | 252,000. |
| | Per cent loans to reserve deposit | 300. | 250. | 186.6 |
| October 2, 1920. | *Reserve Deposit | 21,000. | 31,000. | 133,000. |
| | Loans | 78,000. | 78,000. | 250,000. |
| | Per cent loans to reserve deposit | 371.4 | 251.6 | 187.9 |
| January 5, 1921. | *Reserve Deposit | 20,000. | 30,000. | 130,000. |
| | Loans | 94,000. | 70,000. | 187,000. |
| | Per cent loans to reserve deposit | 470. | 233.3 | 143.8 |
| April 2, 1921 ... | *Reserve Deposit | 20,000. | 28,000. | 121,000. |
| | Loans | 75,000. | 71,000. | 188,000. |
| | Per cent loans to reserve deposit | 375. | 253.5 | 155.3 |
| July 1, 1921 .... | *Reserve Deposit | 18,000. | 29,000. | 123,000. |
| | Loans | 64,000. | 33,000. | 128,000. |
| | Per cent loans to reserve deposit | 355.5 | 113.7 | 104.0 |
| October 1, 1921. | *Reserve Deposit | 18,000. | 32,000. | 127,000. |
| | Loans | 62,000. | 7,000. | 51,000. |
| | Per cent loans to reserve deposit | 344.4 | 21.9 | 40.1 |

* Average for month.

of comparing accommodations granted which is familiar to all bankers. The figures are given at intervals of three months and cover the period of greatest expansion of credit in the United States. It is worthy of note that the total borrowings for all member banks in the agricultural state were on one day nearly five times their total reserve deposits, while the total borrowings of the largest borrowing bank in the Federal Reserve District at the peak were about two and one-half times its reserve deposit. It is also interesting to note that while on October 1, 1921, the largest borrowing bank in the Federal Reserve District was indebteded to the Federal Reserve Bank to the extent of only 22 per cent of its reserve deposit, the total borrowings for all member banks in the agricultural state on the same date were 344 per cent of their total reserve deposits.

It will also be noted from the chart on page 202 showing these percentages,

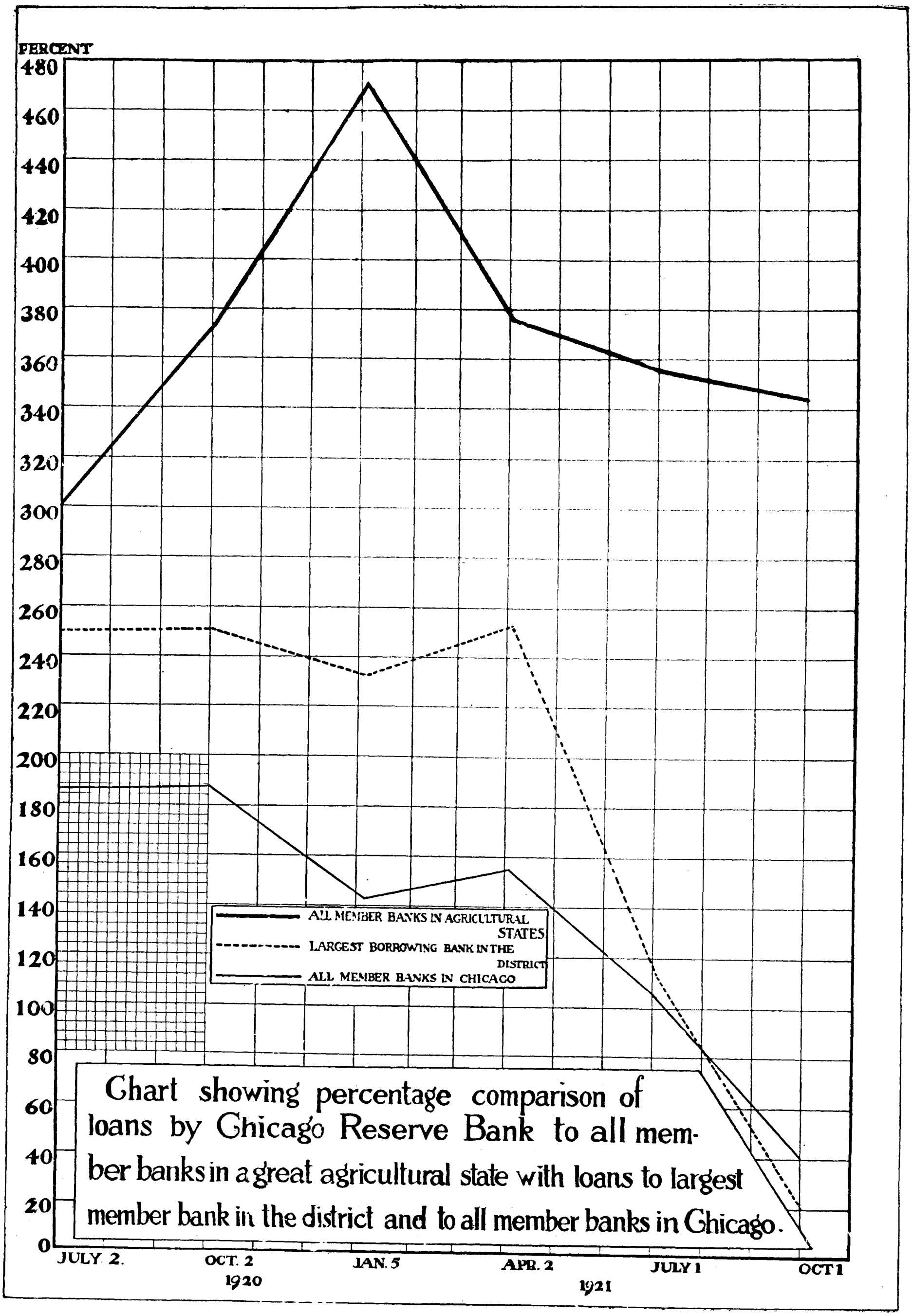


Chart showing percentage comparison of loans by Chicago Reserve Bank to all member banks in a great agricultural state with loans to largest member bank in the district and to all member banks in Chicago.

that since April 2, 1921, there has been great decrease in the amounts owed by the city banks, while the curve for the agricultural state does not show a proportionate decline.

This examination of actual figures makes clear two points: (1) There was no discrimination against agriculture by the Chicago Reserve Bank. Member banks in cities were not favored. (2) Relative, rather than absolute, figures must be used if an accurate idea of the situation is to be had.

# Popular and Unpopular Activities of the Federal Reserve Board and the Federal Reserve Banks

By WILLIAM A. SCOTT
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ON account of the extraordinary conditions under which our Federal Reserve System has been obliged to operate, public opinion towards it has taken peculiar twists and turns. Hopefulness, uncertainty and lack of enthusiasm characterized it at the start, a condition easily explainable by the party controversy which preceded its establishment, differences of opinion regarding the details of the law governing it and conflicts of interest among the people most directly affected by it. Those who had fought and bled for the Aldrich plan were naturally critical of this one and uncertain regarding the manner in which it would work. The state bankers, generally, were hostile towards it because they feared that some of their sources of profits would be jeopardized, and many national bankers did not like its coercive features. The undiscriminating public undoubtedly hoped that it would succeed and was disposed to give it a fair trial.

The outbreak of the European War, three months before the Federal Reserve Banks were ready to begin operations, cleared the atmosphere and smoothed the pathway for them so far as public opinion was concerned, though in other respects it complicated their problems. The financial difficulties which speedily followed made most people thankful for their existence and created a feeling of dependence upon them. No one was disposed to hamper them by criticism.

Before our entrance into the War, their activities do not seem to have attracted public attention to an extent sufficient to arouse either its criticism or its approval. The policy developed during this period of concentrating in their vaults as large a part of the rapidly increasing gold supply as possible by exchanging their notes with the banks for gold, important though it was in checking somewhat the rapidly expanding bank credits and in rendering this mass of the precious metal easily available for any purpose for which it might be needed, seemed to excite curiosity rather than interest.

## WAR COMPULSIONS

With our entrance into the War in April, 1917, the Federal Reserve Banks were called upon to assist the Treasury in its colossal financial operations. As financial agents of the government, they performed the work of executing its plans and measures and, what is more important, so long as the War lasted and for some time thereafter,